

California Fair Political Practices Commission
MEMORANDUM

To: Chairman Getman, Commissioners Downey, Knox, and Swanson

From: John W. Wallace, Assistant General Counsel
Luisa Menchaca, General Counsel

Subject: **Pre-notice Discussion of Amendments to Regulation 18704.2:
Determining Whether Directly or Indirectly Involved in a
Governmental Decision: Interest in Real Property.**

Date: August 26, 2002

I. Historical Background

Section 87100 provides:

“No public official at any level of state or local government shall make, participate in making or in any way attempt to use his official position to influence a governmental decision in which he knows or has reason to know he has a financial interest.”

Section 87103 provides:

“A public official has a financial interest in a decision within the meaning of Section 87100 if it is reasonably foreseeable that the decision will have a *material financial effect*, distinguishable from its effect on the public generally, on the official, a member of his or her immediate family, or on any [economic interest]”....[Emphasis added]

However, what constitutes a “material financial effect” is not defined in the Act. Rather, the Commission defines what is considered “material” for purposes of section 87100 and 87103 through a series of regulations. This regulatory definition, as applied to real property, is the subject of this memorandum.

The concept of “directly involved” real property was introduced to the definition of “materiality” in 1985. Decisions in which an official’s economic interest were “directly involved” were the most obvious conflicts of interest. They were situations where the potential for bias was obvious, such as where a source of income was applying for a permit from the official’s agency, or where the decision was to rezone the official’s own real property. Historically, the Commission applied the strict “one-penny” rule to decisions where the official’s economic interest was directly involved, such as when the official was the applicant or the

official's real property was otherwise directly impacted by the decision. Under that rule, the official was disqualified if the decision had *any* reasonably foreseeable financial effect on his or her property, even one penny's worth.

In 1988, the Commission introduced the concept of decisions in which an official's economic interest was "indirectly involved." With respect to real property indirectly involved in a decision, historically, distance tests were utilized and tied to dollar thresholds. The logic was that the farther the public official's real property was from the real property which is the subject of the governmental decision (the "subject property"), the less likely the financial effect of that decision on the public official's real property would be material. The former version of the indirect materiality standard for real property used three zones around the real property which is the subject property. The inner zone (300 feet or less from the subject property) was subject to the one penny rule. The drafters reasoned that if the real property in which the public official had an economic interest was "very close" to the subject property, then one could presume that the governmental decision would have a material financial effect on the public official's real property.

The second zone went from 300 feet to 2,500 feet and was based on the idea that as the distance from the subject property to the public official's real property *increases*, at some point, the public official's real property is far enough way to presume that a *material* financial effect is not likely. The drafters picked one-half mile as a radius to describe the *inner* boundary of this second zone, and rounded this figure to 2,500 feet. The regulation imposed a \$10,000 materiality threshold for real property in this zone.

Finally, the third zone covered an official's real property when it was more than 2,500 feet from the subject property. Under such circumstances, the financial effect of the decision on the public official's real property was considered material only if there were "specific circumstances" to justify that conclusion.

One other "indirectly involved" materiality standard also existed which was not based on the distance from the public official's real property to the subject property. If the "decision involves construction of, or improvements to, streets, water, sewers, storm drainage, or similar facilities, and the real property in which the official will receive new or substantially improved services," then the financial effects of the decision were deemed material. (Regulation 18705.2(b)(1)(B).)

In 2000, the Commission simplified the indirect standards by collapsing the three zones to the two zones recognized in the current regulation. The current rule is that where the official's real property is within 500 feet of the subject property, the effect is presumed to be material. When the property of the official is beyond 500 feet of the real property subject to the decision, the effect is presumed not to be material. In addition, the Commission made two changes that

were viewed at the time to be cosmetic. In light of the fact that decisions falling within the “500 foot rule” or the “new and improved services” rule were both subject to the “one-penny” materiality standard, the same rule as applied to “directly involved” economic interests, it was decided that these two rules should be recharacterized as “directly involved” and merged with the list of other directly involved decisions.

Consequently, the “new and improved services” rule was moved into the list of “direct standards” as new subdivision (a)(5). However, rather than similarly incorporating the “500-foot rule” into the list, this rule was added to the preamble language in subdivision (a). In addition, for the first time, the list of “directly involved” situations was expressly set forth as a definition of “subject of” for purposes of the regulation. This meant that while in the past the “property subject to a governmental decision” was meant to be a broad, all-inclusive term, after the amendment, the application of the 500-foot rule appeared to be limited to the list of decisions in subdivision (a).

The purpose of the attached amendments is remedial. It is simply to reform the language of the regulation to correspond to the interpretation applied to these rules prior to the most recent amendments. As we noted in October 2001 when this issue was first presented to the Commission, we believe the intent of the Commission in merging the two rules into the direct standard was not to substantively limit their application, but was to place all the rules imposing the same materiality threshold (the one-penny rule), into the same regulation. The proposed regulation accomplishes this.

An associated issue, but not one previously presented to the Commission, is whether the list in subdivision (a) is meant to be exclusive or simply illustrative when it is applied to the official’s own real property. Putting aside problems that have arisen in interpreting the 500 foot rule as incorporated into subdivision (a), the question has also arisen as to whether other decisions affecting the real property of the public official, other than those listed historically under subdivision (a), will still be considered as directly involving the official’s real property. The regulatory language has historically been silent as to whether the list is exclusive. Nothing in the rulemaking file directly addresses this issue. Further, while it has been staff’s position that this is not an exclusive list of what constitutes direct involvement, there are no letters where this has been expressly stated. If the Commission wishes to deal with this issue during this rulemaking process, we would suggest that “including but not limited to” regulatory language be included in the noticed version to highlight the issue for the regulated public.

II. Regulatory Language

While the draft regulation shows a substantial amount of changed text, for the most part the changes are relocation of text rather than substantive changes. We have grouped them under the following:

(a) Consolidating sections

Decision 1: The movement of the 500 foot standard formerly in subdivision (a)'s preamble language to subdivision (a)(1) is the remedial change that deals specifically with the problem at issue in this memorandum. With a few minor clarifying changes, the language has been moved intact into (a)(1). In addition, the preamble language "Real property is the 'subject of the governmental decision,'" which created the unintended consequence, has been removed, and its use is now limited to the distance test. In its place, the former regulation language has been reinserted, which simply specifies that subdivisions (a)(1) through (6) are situations where the officials' real property is directly involved.

In addition, language formerly set forth in the redevelopment section (a)(5) after renumbering has been moved to (a)(1), again essentially intact. This is because this language is an interpretation of the 500 foot rule.

Decision 2: The second relocation amendment simply moves language formerly set out as (a)(6), into renumbered (a)(2). The moved language is an elaboration of the zoning concept in renumbered (a)(2) and more appropriately belongs in that section.

(b) Clarifying Changes

In several subdivisions (such as renumbered (a)(3)), references to "such real property" have been replaced with a more explicit and clear reference to "the real property in which the official has an interest." (See also renumbered (a)(6).)

(c) The Exceptions

Finally, two exceptions, at **Decision 3**, to these "direct effect" rules that were formerly merged in with the standards have been separated and placed in another subdivision, new subdivision (b). This change was necessary to clarify that the two exceptions not only applied to the specific subdivisions in (a) for which they were written, but also the general distance test in (a)(1).

III. Staff Recommendation

Staff recommends that the Commission approve the amendments to regulation 18704.2 for adoption.

Appendix 1: Former Regulation 18702.1: Material Financial Effect: Official's Economic Interest is Directly Involved in the Decision.

Appendix 2: Former Regulation 18702.3: Material Financial Effect: Ownership Interest in Real Property Indirectly Involved in the Decision.

Appendix 3: Conflict of Interest Regulations Improvement Project Phase 2 Amendment to Regulation 18704.2